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REAL ESTATE OUTLOOK

November
December 1987

A Monthly Forecast for the Economy and Real Estate

FORECAST SUMMARY

- The total output of goods and services, after adjusting for inflation, increased at an annual rate of 3.8 percent in the third quarter. Consumption spending and business fixed investment were the strongest sectors in the economy in that quarter.
- The stock market crash is expected to reduce consumer spending over the next few quarters. Solid growth in net exports due to large gains in U.S. exports will replace consumption spending as the strongest contributor to fourth quarter real GNP growth.
- Fears of high inflation are said to have been a possible cause of the stock market crash. These fears appear to have dissipated and consumer prices are expected to increase by only 4.3 percent in the current quarter, and 4.1 percent in 1988.
- The bond market rally has pushed down yields on long term U.S. Treasury securities by as much as 150 basis points. Mortgage rates are expected to follow suit, trending down throughout 1988.
- Sales of existing single-family homes could reach 3.21 million units in 1988, 3 percent below the projected 1987 rate of 3.32 million units. This expected decline is partly due to losses of wealth from the stock market crash which will be offset by declines in mortgage interest rates.

IN THIS ISSUE

- Economic Commentary: AN ILL WIND, by John A. Tuccillo
- Outlook for the Economy & Real Estate
- Secondary Market Outlook, by Mary A. Fruscello
- Special Topic: The Homebuying and Selling Process, 1987

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AN ILL WIND:
Economic Commentary

by
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It is an ill wind that blows no good, but the stock market debacle of the past several weeks emphatically does not qualify. Although we've seen a great deal of wealth wiped out, the shift of funds from stocks to bonds – a full-blown flight to liquidity and quality – will push interest rates down through the end of 1987 and revive what had become a disturbingly sluggish housing market. But like the mild heart attack sent as a warning by nature, the market drop is signaling some deeper sickness within the economy that needs to be cured if the patient is to live a long healthy life.

By now, we've all read about the ins and outs of the big Crash of '87: how nearly $1 trillion in wealth was wiped out; how investment firms became completely overwhelmed by orders; how most of middle America was, at least initially, unaffected; how a yuppie stockbroker differs from a pigeon in that the pigeon can still make a deposit on a BMW. But look at this from the point of view of real estate. The losses in the stock market triggered a bond market rally that has pushed both long- and short-term rates down. Adding to this has been the actions of the Federal Reserve in flooding the economy with cash in an effort to avert the catastrophes of 1929. As a result, long-term Treasuries fell by about 125 basis points in a ten-day period, federal funds are trading a full point below their September highs and mortgage rates are headed south.

This will be good for housing for two reasons. First, lower interest rates, especially in a growing economy, will necessarily stimulate home sales and construction. But, also, mortgage rates have been trending upward since March, with a particular burst in September. The break in that progression that we are now witnessing will unleash the demand that had been stifled all summer. We ought to see a fourth quarter of greater-than-expected housing activity.

But how can housing thrive while wealth is being destroyed? Clearly the stock market plunge destroyed the capability of many households to buy a house and crippled the confidence of others. I don't believe that this is a problem, at least in the short run. In fact, relatively few Americans were caught under the falling Dow. On a year-to- year basis, the DJIA is virtually unchanged from October 1986. Moreover, many losses took the form of declines in the value of their pension funds, a factor which enters only weakly into current consumption choices. Should the market disaster permeate the economy and generate a recession, housing will suffer in the first half of 1988. For now, consumer confidence appears to be holding, and interest rates will dominate housing for the remainder of 1987. The prospects for 1988 will become clearer as the stock market sorts itself out. Those prospects will hinge on whether policy makers in Washington and the rest of the world heard the message of Wall Street. There are some very real problems with the American economy, and those who predict the future by playing the stock market have clearly expressed their doubts that the current expansion can survive those problems. Right now, our current account deficit is equal to 3.6 percent of GNP. The world will eventually force us to zero-out that balance; either we will produce more and consume less, or the international markets will drive the value of the dollar steadily lower.

On the domestic side, our Federal budget deficit is still out of control. Even though the fiscal year 1987 deficit fell to $148 billion, there has been no real movement to close the gap fully. The longer the deficit persists, the greater are the chances that interest rates will remain high to attract foreign capital. Wall Street knows, and has clearly stated, that the perpetuation of the two deficits cannot exist simultaneously with a consumption-based economic expansion. Simply put, our spending spree has been financed by foreign funds, and the IOUs are coming due.

Without real solutions, the day of reckoning will inexorably approach. Soon there will be no options except for a period of higher taxes and lower real consumption. But like Scrooge on Christmas Eve, we have seen what might be and still have time to change. The dollar will likely fall by another 10 percent against major currencies before year-end. If that is accompanied by a real reduction of the federal deficit by the President and the Congress of $40-50 billion, then the markets will calm and the basic strength of the economy will reassert itself. But that deficit reduction must occur as part of a longer range program of fiscal discipline if it is to convince financial markets that the future is bright.

A former chairman of the Fed characterized his role as the guy who takes away the punchbowl just when the party's getting good. Well, the party's not yet over, but we need to take away the punchbowl and bring out the coffee urn.

Outlook for the Economy and Real Estate

Now that the bull has stopped charging, economic growth will be slower and its composition much different from the surprisingly strong third quarter real GNP annual growth rate of 3.8 percent. The third quarter reading on the health of the U.S. economy painted an image of a renewed level of real growth drawing from large gains in exports, stronger consumer spending, and greater business fixed investment. Compared to the 3.4 percent annual growth rate of the first half of 1987, the economy might have been positioning itself for another growth surge.

September seemed to be a good month for economic indicators: personal income advanced 0.7 percent, nondefense durable goods orders jumped 1.7 percent and inflation (as measured by the GNP deflator) increased at only a 2.4 percent annual rate during the third quarter, compared to 3.5 percent in the second.

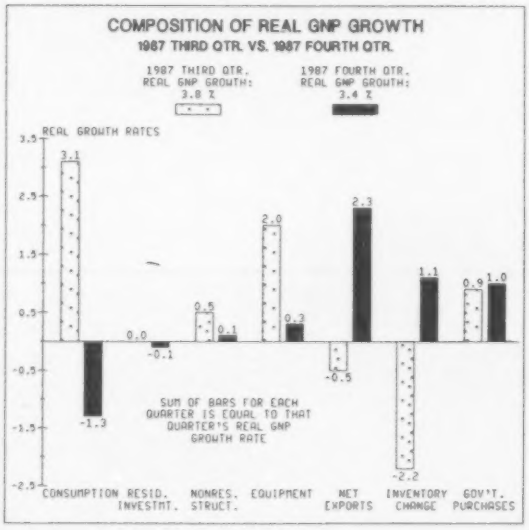
Changing Composition of Real GNP Growth

As always, numbers play tricks on the eyes and ears of economists. For example, the 16.5 percent annual rate of growth in the third quarter volume of U.S. exports was actually offset by an equal percentage rise in import volume. And since import volume is approximately one-third larger than export volume, the equal percentage rise in imports actually pried open the trade gap a bit further. Responding to tensions in the Persian Gulf, a huge petroleum inflow of $19.3 billion explained most of the import rise but not all. Nonpetroleum imports continued to increase in the third quarter, as America's appetite for foreign goods lingers on despite rises in import prices. The result was a negative contribution from net exports to real GNP growth (see Graph). Despite this setback in net exports, trade is expected to resume its positive contribution to GNP growth in the fourth quarter and into 1988, helping to offset the expected widespread weakness in other sectors. Next year could be remembered as the year in which the trade gap fell, if the effect of the stock market crash on current spending is enough to dissuade consumers from the more expensive imported goods and in favor of U.S. products.

Consumer spending has been all but ruled out as a source of economic growth in the current quarter. The stock market crash is expected to be the straw that breaks the debt-laden consumer's back and could force a return to a more normal rate of personal savings. The fat 4.8 percent rise in consumer spending during the third quarter borrowed from this quarter's auto sales, setting up yet another payback period for the auto industry. Further, the 0.7 percent September gain in personal income masks the fact that consumer incomes adjusted for inflation are virtually unchanged over the past year. Coming only weeks before the beginning of the retail industry's make or break quarter, the effect of the stock market crash will be felt immediately.

So, while the economy had been gaining on the basis of export growth, consumer spending and business fixed investment, the latter two are not as likely to contribute positively to real GNP growth in the next few post-crash quarters.

Two responses in consumer spending to the stock market crash are expected. First, the loss of $1 trillion in wealth will have a direct effect on the 20



percent of consumers who were actively investing in the stock market. Many of these consumers are on the high end of the income scale and account for a larger share of consumption than their small share of the population might suggest. It is important to keep in mind that that the loss of $1 trillion in wealth only represented wealth earned since about the beginning of 1987, and not since the 1982 start of the bull market.

The indirect effect centers around how consumers not in the stock market will react. Consumer confidence at present seems to be holding steady. The fact that the homeownership rate in the third quarter of 1987 was 64.0 percent compared to the 47.8 percent rate of 1930 suggests that the total distribution of personal wealth is skewed more toward real estate than it was during the Great Depression. This

greater proportion of assets in real estate is complemented by a far more secure financial system backed up by extensive deposit insurance programs. These two factors in particular are keys to understanding the steadiness of consumer confidence.

Net exports are expected to provide the steadiest source of real GNP growth in the current quarter, producing an annual rate of about 3.4 percent. After a sluggish first half in 1988, real GNP growth could rebound in the second half on the strength of buoyant consumer spending. This could bring the average annual rate of real GNP growth to 2.4 percent next year. As with the other sectors, it is too soon to tell if capital spending plans of businesses have been revised down across all sectors. Unofficial indicators and surveys suggest that business executives for the most part feel confident that consumers will not overreact to the stock market downturn by immediately postponing all spending.

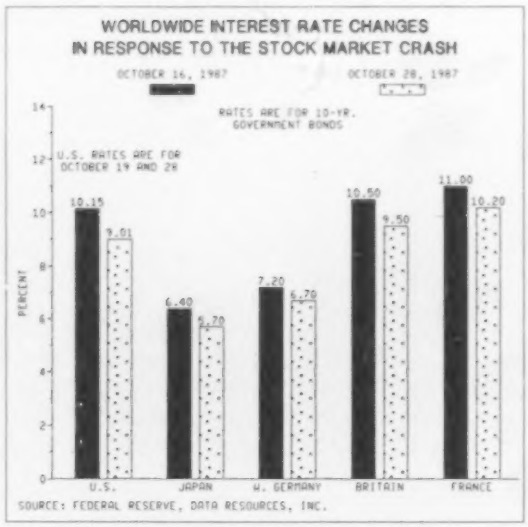
These developments generally portend good news for consumer price inflation in 1988. The CPI is expected to increase by 4.1 percent in 1988, a downward revision from the last forecast. A broader estimation of inflation, the GNP price deflator, is expected to rise by 3.1 percent in 1988, also revised down from the previous forecast. A slower rate of growth in total output forced by the expected weakness in consumption explains most of the lower rate of inflation. The lackluster output growth could nudge the employment rate up over 6 percent in 1988. Nevertheless, modest wage gains are expected in 1988 after many quarters of little or no change.

Monetary Policy and Interest Rates

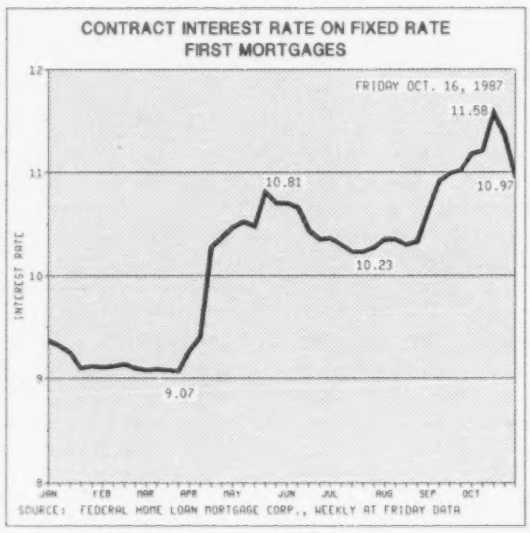
As the Dow Jones Industrial Average plummeted, so too fell the high inflationary expectations of financial market participants. This has granted Chairman Greenspan greater leeway in conducting a monetary policy conducive to stable economic growth. In fact, the Fed's quick move to increase liquidity was just the assurance many investors needed. This has helped satisfy the tremendous demand for cash and has led many major banks to announce hefty reductions in the prime rate.

But at the same time, the Chairman must also pursue a monetary policy which keeps the spread between the interest rates on dollar denominated assets and those on comparable foreign investments wide enough to keep large amounts of foreign capital flowing into the domestic economy. (see Graph) Currently, world interest rates are dropping together because of the stock market crash. These rate differentials must be maintained, particularly to continue to attract capital from Japanese investors.

The conduct of monetary policy with respect to these foreign capital inflows is particularly important to avoiding a recession. The Administration and Congress are working out a budget compromise that will reduce the share of economic growth due to spending by the Federal Government. This contractionary fiscal policy will have to be offset by a more expansionary monetary policy that encourages world interest rates to decline and domestic investment and private spending to increase.



This policy shift from anti-inflation to anti-recession carries good news for the housing industry in the form of lower interest rates. Already the flight to quality (from stock into bonds) has touched off a bond market rally that has driven yields on long-term Treasury securities down by 150 basis points. The rate on a 30-year fixed rate mortgage could drop to 10.6 percent in the current quarter before seesawing throughout 1988 to an annual average of 10.8 percent.

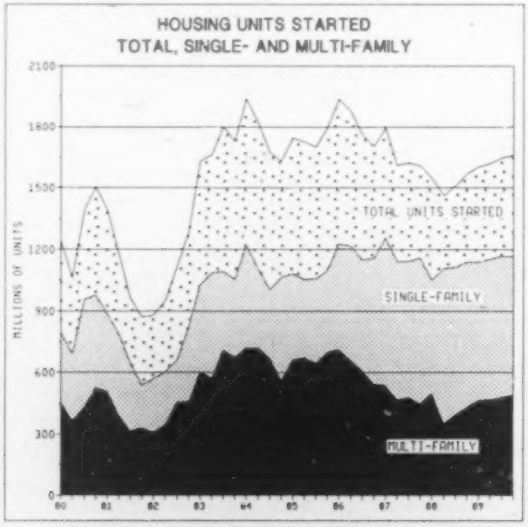


Real Estate Markets

Housing Starts

Total housing starts in September reached an annual rate of 1.669 million units, up 4.4 percent from the revised August annual rate of 1.598 million units. The September 1987 rate was 1.2 percent short of the September 1986 rate of 1.689 million units.

September single-family units were started at an annual rate of 1.168 million units, 5.1 percent above the revised August annual rate of 1.111 million units. The September 1987 single-family start rate was 4.0 percent below the September 1986 rate. Higher interest rates continued to hold down single-family starts activity. Single-family starts are forecast to reach an average annual rate of 1.158 million unit rate in the fourth quarter of 1987. Single-family starts could fall

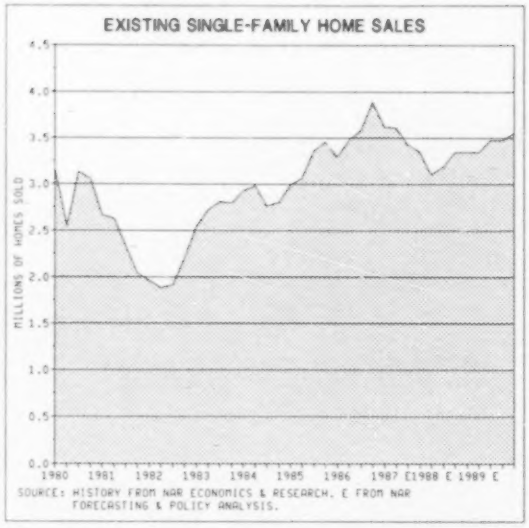


to a 1.102 million unit average annual rate in 1988.

Multi-family housing units were started at an annual rate of 501 thousand units in September, a 2.9 percent gain over the August annual rate of 487 thousand units. The annual rate of multi- family starts was 11.5 percent below the September 1986 start rate. Multi-family units are expected to be started at an average annual rate of 451 thousand units in the current quarter, before slowing to an average annual rate of 420 thousand units in 1988.

Existing Home Sales

Existing single-family homes were sold at a seasonally adjusted annual rate of 3.45 million units in September, up 1.2 percent from the revised August rate of 3.41 million units. Seasonally adjusted existing single-family home sales rates rose in all regions of the country with the exception of the West region. In that region, the existing home sales rate declined 5


EXISTING SINGLE-FAMILY HOME SALES
MILLIONS OF HOMES SOLD
SOURCE: HISTORY FROM NAR ECONOMICS & RESEARCH. E FROM NAR FORECASTING & POLICY ANALYSIS.

percent from the August rate of 600,000 units to the September rate of 570,000 units. The Northeast annual rate rose from 670,000 units in August to 690,000 units in September, a 3 percent increase. Existing homes in the Midwest region were sold at an annual rate of 880,000 units, up 2.3 percent from the August annual rate of 860,000 units. In the South, existing home sales reached an annual rate of 1.31 million units, also a 2.3 percent rise above the August rate of 1.28 million units.

The forecast for total existing single-family home sales has been revised down from the September/October REO forecast of 3.32 million units for 1988, to 3.21 million units, a 3.6 percent decline. Most of this strength in existing home sales derives from mortgage rate declines and the assumption of no prolonged and serious decline in consumer confidence. Existing single-family home sales are expected to fall somewhat because of the stock market crash. The extent of the reduction will be tempered by the expected decline in lower mortgage rates brought about by a bond market rally. The strong demand for fixed-income investments like bonds has driven their prices up and their yields down. [For further information, read "Secondary Market Outlook" in this issue.]

The median sales price of an existing single-family home sold in September fell slightly to $84,900, a 0.2 percent decline from the $85,100 August median sales price for an existing home. This small decline is more than likely a seasonal decline that is characteristic of this not seasonally adjusted price data. In 1987, the median sales price is expected to average $84,600, a 5.4 percent rise over the $80,300 median sales price of 1986. Factoring in the expected 3.7 percent annual rate of inflation for 1987 (year-over-year percent change) means that existing home prices will on average experience a real increase of almost 2 percent.

New Home Sales

Some of the relative strength in existing home sales is due to reduced activity in the new home sales market. Sales of new single-family homes are expected to fall to 630 thousand units in 1988 before recovering somewhat to 670 thousand units in 1989. With most of the data on 1987 already reported, it appears that new home sales will total 681 thousand units in 1987, down 0.3 percent from 1986.

The median sales price of a new home sold in September rose to $115,600, an 8.5 percent increase over the August median price of $106,500. New homes have continued to rise in price despite declines in new home sales volume. New homebuyers remaining in the market after the rises in mortgage interest rates during the Spring and early Fall are likely to be higher-income homebuyers who typically buy the more expensive new homes. New home prices could rise by 4.3 percent in 1988 to $109,900, as this trend continues.

RISKS TO THE FORECAST

In the previous forecast, the interplay of the value of the dollar, the rate of inflation and the attractiveness of U.S. real interest rates to foreign investors was given as a potential threat to the housing estimates made therein. That caution applies to this forecast as well. However, the stock market crash has increased the pressure on monetary authorities around the world to minimize the uncertainty engendered by the complex relationship of the dollar, inflation and real interest rates.

Another critical viewpoint to take when evaluating this forecast is to consider that consumer spending could take longer to recover than the third quarter of 1988, as assumed. If it does, then the likelihood of a reeession in late 1988 is slightly higher, but by no means is it a certainty.

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Secondary Market Outlook

by
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A dramatic illustration of the advantages and disadvantages of the close link between the mortgage and capital markets, and the dependency of home buyers and sellers on stability in the mortgage securities markets, occurred with the stock market debacle in October. As the equity markets plunged, investors began a classic "flight to quality," abandoning stocks for Treasury notes and bonds. The immediate effect on the mortgage backed securities market was a price decline, followed quickly by investor realization that for most pass-through securities, the quality of the guarantee is the same or substantially the same as that for Treasuries. As a result, mortgage backed securities have participated in the rally in bond prices, producing lower yields to investors.

At the same time, however, the highly touted liquidity of the mortgage backed securities market took its second hit since April. Most major investment banking houses stopped making bids for securities at some point during the week of Black Monday, and in the following week traders remained reluctant to position in securities, preferring to take sell orders subject to their finding buyers.

For housing and homebuyers, the effects of these conditions are likely to be mixed. Investor preference for bonds, including mortgage backed securities, as well as the Fed's less restrictive monetary policy, can translate into lower mortgage interest rates. Many mortgage lenders, however, are faced with an unpleasant reality in this scenario. Those who have purchased forward commitments to sell mortgages in the securities market are likely to be faced with borrowers who walk away from commitments at rates now above market, forcing lenders to take losses from their mandatory delivery securities sales positions. Unfortunately, rising rates had already reduced volume, making the decline less welcome than might have been expected. There is also some indication that continued erratic liquidity in the mortgage securities market may be due to anticipation of supply problems stemming from a slowdown in origination volume as consumers look for reassurance about the economy before buying homes.

The liquidity problems in the fixed rate securities market come at a time when problems with ARMs and ARM securities are beginning to surface. As mortgage rates began moving up this year, borrowers predictably demonstrated a decided preference for adjustable rate mortgages. Since early spring, ARM popularity as reported in the National Association of Realtors Survey of Home Financing Transactions grew from 7 per cent of first mortgage originations in April to 33 per cent in September.

The move from fixed rate to adjustable rates loans has been relatively smooth, with no financing gaps while lenders developed an alternative product. However, there have been two disturbing aspects to the rapid shift to ARMs: the limited progress towards standardization of loan terms, and the disappointing reception by the investment community for ARM mortgage backed securities.

When ARMs became nationally popular during the high rate period of the early eighties, there were no FHA, Freddie Mac or Fannie Mae ARM programs. Left to the forces of an unstructured and competitive marketplace, lenders created a plethora of loan terms, indices and pricing structures in their scramble to lure borrowers into a financing technique that would allow them to qualify for loans during that period of unprecedented high interest rates. Since those heady days of highly creative mortgage lending, the conventional wisdom has been that lenders are now sensitive to the pitfalls of a fragmented mortgage market and an illiquid product line.

Yet the picture of ARM lending since mortgage interest rates began their upward march in late spring is not encouraging. True, there has been some standardization of basic ARM terms, such as index, adjustment period and amortization rates. The Home Financing Transactions Survey indicates that the market has largely settled on two ARM indices--U.S. Treasury constant maturity and the FHLBB cost of funds--adjustment periods of one or three years, and no negative amortization. But in the rush to offset declining loan volume as refinance activity abated, many portfolio lenders began originating ARM product at below market prices, and the market began to return to the chaos of 1982-83.

Teaser rates--initial interest rates well below the fully indexed level mandated by the ARM index rate and margin--are again widely

reported, creating several potential problems. Portfolio lenders are using discount pricing to trade current yield for the interest rate sensitivity of ARMs. They are offsetting their losses by using an accounting method that (until the end of 1987) permits full recognition of point income when the loan is booked. Unfortunately, the teaser rate strategy in some cases produces loans that may take many years, if ever, to reach market rates of return.

If borrowers retain their new found preference for ARMs, the effect of such price cutting will be felt in the mortgage market much more quickly. Mortgage bankers are finding themselves unable to compete with the ARM teaser rates, because the prices they receive for such loans in the secondary market are not adequate to produce a break-even spread on the loan sale. For borrowers, this could produce a short-lived windfall in mortgage terms, followed by a financing scarcity as some mortgage sources disappear.

Even more disturbing than the problems in the ARM origination market, however, is the lukewarm reception by investors to the ARM securities that have been introduced. The GNMA ARM has had only modest volume, in part because of the arbitrary limitations that until recently have been placed on FHA ARM commitments available to lenders, restricting origination volume to unmarketable levels. Even the more recent Freddie Mac ARM security is not highly visible in the trading markets.

Market observers attribute some of the investment reluctance to the lack of volume outstanding. There have been only $4 billion Freddie Mac ARMs issued, and only $2.6 billion in GNMA ARMs. Many of these securities, once issued, do not trade, an indication that, unlike the fixed rate security, the ARM security investor base is narrow and not substantially different from that of the ARM mortgage itself. Without an active resale market, ARM securities cannot offer the liquidity that attracts buyers.

An even greater concern, however, is the lack of analytical tools to value ARM securities. Pricing models vary as widely as they did three years ago; they are complex and (in some cases) highly arbitrary. Investors, lacking confidence in the pricing approaches available, have not rushed to these new products.

Also contributing to the spotty liquidity in ARM security trading is the lack of an effective hedging vehicle. With no instrument to offset risk, traders are reluctant to position in ARM securities, hindering the development of an active trading market.

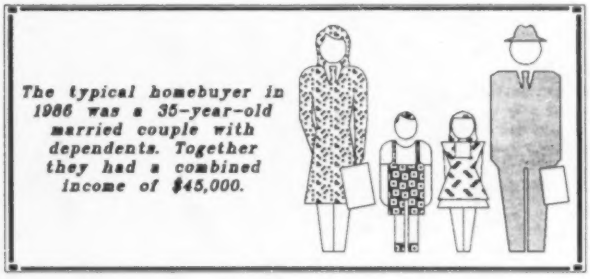
The disappointing progress in ARM standardization reflects the highly cyclical nature of the product. When rates are low, minimal borrower and investor interest in ARMs discourages attention to the limitations of this new and somewhat untested product. A protracted interest rate rise may provide enough time for the market to focus on solving critical problems such as pricing techniques to facilitate trading and liquidity.

For the present, however, investors are unable to evaluate ARMs with techniques conducive to rapid trades. The result is that the primary ARM market is not being driven by secondary market needs, and as we have learned in the past few years, secondary market requirements must become the focus if we are to have efficient markets and a steady supply of affordable funds to borrowers. From that perspective, and given the disruption in liquidity for fixed rate mortgage securities, continued volatility in the capital markets may prove a mixed blessing for housing and homebuyers, as it deprives mortgages of the liquidity essential to make reasonably priced financing available.

SPECIAL TOPIC:

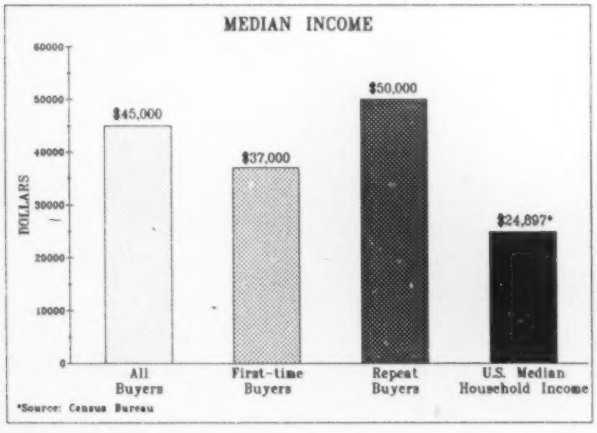
THE HOMEBUYING AND SELLING PROCESS: 1987

A recently published report titled The Homebuying and Selling Process: 1987 (NATIONAL ASSOCIATION OF REALTORS®, Economics and Research Division), provides a nationwide profile of the homebuyer, the home purchase process, the homeselling process, and a close look at 12 metropolitan housing markets. The report is based on a sample


The typical homebuyer in 1986 was a 35-year-old married couple with dependents. Together they had a combined income of $45,000.

of nearly 4,000 homebuyers who purchased homes during the last six months of 1986.

While it is interesting to take a snapshot look at the typical homebuyer of 1986, a closer look reveals a great deal of variation in the homebuying public.



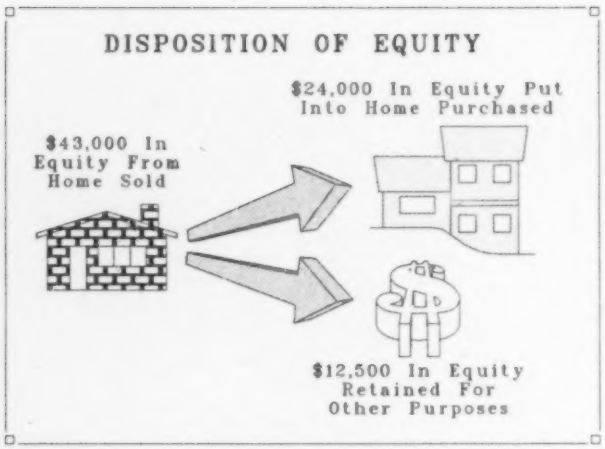
As would be expected, first- time buyers are, on average, about 10 years younger than repeat buyers. Two-thirds of first-time buyers are in the prime homebuying years between the ages of 25 and 34 compared to only 30 percent of repeat buyers. Over one-third of repeat buyers are in the 35 to 44 year old age group where one finds the heaviest concentration of families with higher incomes and an increased need for space. The median age of all homebuyers is 35.

The income data demonstrates why housing affordability is such a vital social issue in the United States today. Ninety percent of first-time buyers earned more than the national median household income ($24,897) in 1986. The median income of first-time buyers was $37,000 – over $12,000 more than the national median household income. The income data for repeat buyers is equally striking: the median income of repeat buyers is approximately twice the median income of all households, and most repeat buyers earned more than the median income of all households. This is remarkable since it occurred at a time when the Housing Affordability Index, a widely used measure of housing affordability, was well over 100 and had been improving for over six years.

Seventy-one percent of all homebuyers surveyed were repeat buyers. Compared to first-time buyers, they are generally older, have higher incomes, and buy more expensive homes. But there are other findings concerning repeat buyer purchasing behavior that may be of interest.

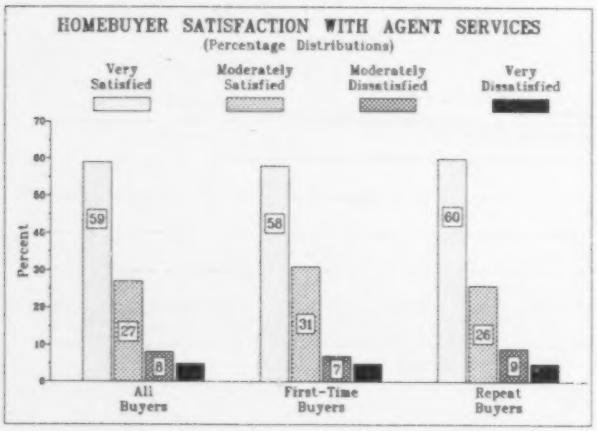
Sixty-four percent of repeat homebuyers in the survey sample were trading up – buying a home worth at least 10 percent more than the home they sold. The median home price paid by trade-up buyers was $115,000, an increase of $39,500 over the home they sold. Seventeen percent of repeat buyers bought homes in the same price class as the home they sold and 19 percent were trading down – buying a home worth at least 10 percent less than the home they sold. The difference in the median price between the homes trade-down buyers purchased and the homes they sold is remarkable: $63,000. Data on trade-down buyers is influenced by older buyers who often sell large detached single-family homes and purchase either small detached single-family homes, townhomes, or apartment condominiums. In fact, 30 percent of buyers age 55 to 64 and 32 percent of buyers age 65 and over claimed their preference for a smaller home was a major reason for moving.

This aspect of trading patterns raises the question of the disposition of equity. Equity from a previous home was cited most frequently by repeat buyers as


DISPOSITION OF EQUITY
$24,000 In Equity Put Into Home Purchased
$43,000 In Equity From Home Sold
$12,500 In Equity Retained For Other Purposes

a source of downpayment on another home. The median amount of equity put into a home purchase by repeat buyers, however, was significantly less: $24,000. The difference is equity retained for other purposes; for example, closing costs on the property purchase, relocation expenses, making ancillary purchases, home improvements, or investments.

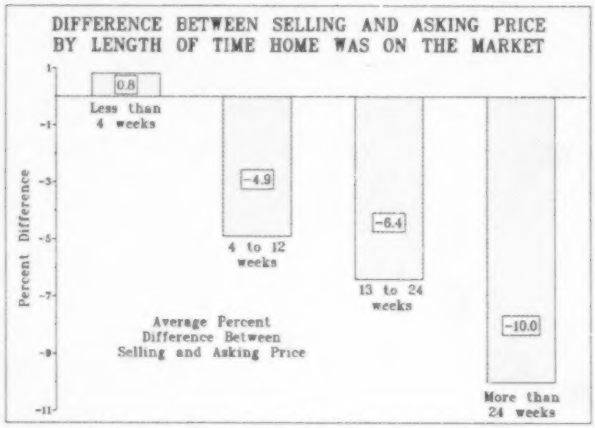
One aspect of the homebuying process that is critically important to real estate professionals is the level of homebuyer satisfaction with the services provided



by real estate agents. The survey results indicate that 86 percent of the homebuyers were satisfied with the services provided by their real estate agents. In fact, 59 percent indicated they were very satisfied. Nearly three-quarters of the survey panelists claimed they would be willing to use their agent again if the opportunity presented itself while only one respondent in 10 said he would not.

As noted above, 71 percent of the national survey panelists were repeat buyers. These experienced homebuyers represent a primary source of information about the homeselling process. One aspect of this process that may interest Outlook readers concerns the difference between the selling and asking price of homes.

The basic forces of supply and demand are evident in survey results that compare the average percent difference between the actual selling prices of homes and the asking prices. On average, homes that were on the market for less than four weeks actually sold for slightly more than the original asking price. However, as the length of time a home was on the market increased, so did the difference between the asking price and the selling price. Homes on the market for more than 24 weeks sold for an average 10 percent less than the asking price.



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U.S. ECONOMIC OUTLOOK

	QUARTERS							YEARS				
	Actual		Forecast					Actual		Forecast		
	1987.2	1987.3	1987.4	1988.1	1988.2	1988.3	1988.4	1989.1	1985.0	1986.0	1987.0	1988.0	1989.0
AGGREGATE ECONOMY													
Gross National Product (billions of dollars)	4445.1	4512.0	4576.2	4627.6	4680.7	4758.4	4840.2	4937.2	4010.3	4235.0	4477.8	4726.7	5070.0
% Change	6.3	6.2	5.8	4.6	4.7	6.8	7.1	8.3	6.3	5.6	5.7	5.6	7.3
% Change (w/out inflation)	2.5	3.8	3.4	1.5	1.0	2.9	3.3	3.8	3.0	2.9	2.8	2.4	3.0
Consumer Prices (CPI)	4.9	3.9	4.3	3.9	3.8	4.1	4.4	4.9	3.6	1.9	3.7	4.1	4.6
GNP Deflator	3.5	2.4	2.2	3.1	3.6	3.8	3.6	4.3	3.2	2.6	2.9	3.1	4.1
Unemployment Rate (%) (civilian)	6.2	6.0	6.0	6.0	6.2	6.2	6.2	6.0	7.2	7.0	6.2	6.1	5.9
Civilian Employment-Household Basis (millions)	112.2	112.9	113.4	113.8	114.1	114.4	114.9	115.5	107.2	109.6	112.4	114.2	116.2
% Change	3.4	2.4	1.8	1.6	0.9	1.3	1.6	2.1	2.0	2.3	2.6	1.7	1.7
Mfg. Capacity Utilization	80.5	81.5	82.0	82.4	81.9	82.1	82.4	82.9	80.3	79.7	81.0	82.2	82.9
Domestic Auto Sales	7.0	8.0	6.1	6.7	7.2	7.2	7.5	7.4	8.2	8.2	7.0	7.1	7.4
Federal Tax Receipts (NIPA) as % of GNP	0.21	0.20	0.20	0.20	0.20	0.20	0.20	0.21	0.20	0.20	0.20	0.20	0.21
Federal Expenditures (NIPA) as % of GNP	0.24	0.24	0.24	0.24	0.24	0.23	0.23	0.23	0.25	0.24	0.24	0.24	0.23
Deficit(NIPA)	-139.3	-148.9	-167.2	-168.9	-156.9	-162.1	-155.0	-128.0	-196.0	-204.7	-161.5	-160.7	-122.6
as a % of GNP	-3.1	-3.3	-4.1	-3.6	-3.4	-3.4	-3.2	-2.6	-4.9	-4.8	-3.6	-3.4	-2.4
REAL ESTATE MARKETS													
HOME SALES													
Total Single-family Home Sales (1000, single-family resales plus 97 percent of single-family starts)	4.718	4.536	4.473	4.122	4.263	4.326	4.407	4.447	4.254	4.717	4.455	4.279	4.581
Percent change -- year ago	1.3	-3.5	-10.8	-14.7	-9.6	-4.6	-1.5	7.9	8.6	10.9	-5.6	-3.9	7.0
Existing Single-family Home Sales (1000)	3.610	3.430	3.349	3.103	3.188	3.247	3.303	3.343	3.214	3.565	3.316	3.210	3.460
Percent change -- year ago	3.8	-4.4	13.9	-14.2	-11.7	-5.3	-1.4	7.7	12.1	10.9	-7.0	-3.2	7.8
Housing Starts	1611.7	1621.7	1608.7	1547.6	1461.7	1508.8	1569.4	1602.7	1742.3	1819.2	1659.2	1521.9	1631.7
Percent change -- year ago	14.2	7.8	5.5	13.8	-9.3	-7.0	2.4	3.6	1.4	4.4	-8.8	-8.3	7.2
Single-Family Units	1142.0	1140.7	1158.3	1050.9	1107.9	1112.7	1138.0	1137.9	1072.6	1188.1	1174.2	1102.4	1155.6
Percent change -- year ago	6.2	-0.8	0.0	-16.3	-3.0	-2.4	-1.8	8.3	-2.4	10.8	-1.2	-6.1	4.8
Multi-Family Units	469.7	481.0	450.5	496.7	353.8	396.1	431.4	464.9	669.7	631.2	485.0	419.5	476.2
2-4 Family Units	73.0	58.0	54.3	59.9	42.7	47.8	52.0	56.1	93.4	85.4	66.3	50.6	57.4
Percent change -- year ago	-9.9	-24.3	-38.3	-25.1	-41.6	-17.6	-4.2	-6.4	-23.3	-8.6	-22.3	-23.7	13.5
5+ Family Units	396.7	423.0	396.1	436.8	311.1	348.3	379.4	408.8	576.2	545.8	418.7	368.9	418.7
Percent change -- year ago	-31.6	-20.4	-13.1	-4.8	-21.6	-17.7	-4.2	-6.4	5.5	-5.3	-23.3	-11.9	13.5
New Single-family Home Sales (1000)	674	674	650	634	610	620	655	679	749	685	681	630	700
Percent change -- year ago	-15.1	-1.7	-8.6	-12.3	-9.5	-8.0	0.8	7.1	17.2	-8.5	-0.6	-7.5	11.1
Mobile Homes Shipped (1000)	227	237	242	232	241	244	250	252	283	249	235	242	258
HOME PRICES													
Existing Home Prices - Median ($1000)	85.1	85.0	84.1	86.2	88.5	89.8	89.7	92.3	75.5	80.3	84.6	88.6	93.0
Percent change -- year ago	2.8	5.3	4.9	2.3	4.0	5.6	6.7	7.1	4.3	6.4	5.4	4.7	5.0
New Home Prices - Median ($1000)	103.5	108.7	112.0	110.0	105.0	107.6	105.9	108.7	84.3	92.0	105.4	109.9	114.9
Percent change -- year ago	12.6	16.2	17.7	13.0	1.5	-1.0	-5.4	-1.2	5.5	9.1	14.6	4.3	4.5
FINANCIAL MARKETS													
Long-Term Interest Rates (%)													
30-year Fixed Rate Mortgage (FHA Secondary)	10.3	10.7	10.6	11.0	10.8	10.6	10.4	10.5	12.2	9.9	10.1	10.7	10.6
1-year ARM (without buydown)	8.1	8.3	8.2	8.4	8.4	8.2	8.2	8.2	7.6	7.9	8.2	8.3	8.2
Corporate AAA Bond Rate	9.2	9.8	10.2	9.8	9.5	9.5	9.5	9.6	11.4	9.0	9.4	9.6	9.6
Government Bond Rate	8.5	9.1	9.1	8.6	8.2	8.3	8.2	8.4	10.8	7.8	8.6	8.3	8.6
Federal Funds Rate	6.7	6.8	7.1	6.5	6.3	6.4	6.6	6.7	8.1	6.8	6.7	6.4	6.9
3-month T-Bill Rate	5.7	6.0	6.0	5.3	5.2	5.3	5.4	5.5	7.5	6.0	5.8	5.3	5.7
Prime Rate	8.0	8.4	8.9	8.4	8.0	7.6	7.4	7.4	9.9	8.3	8.2	7.8	7.7
Discount Rate	5.5	5.7	5.8	5.6	5.1	5.1	5.2	5.2	7.7	6.3	5.6	5.2	5.3
Money Supply (M1)(% change)	6.5	-0.1	5.6	8.0	7.8	7.2	7.4	6.7	11.9	15.2	6.5	7.6	6.2
Value of the U.S. Dollar (Trade-Weighted Avg.)	97.0	98.7	96.4	95.4	92.9	91.4	89.9	143.2	143.2	112.3	98.0	92.4	89.0
Percent Change	-11.1	7.2	-8.7	-4.3	-9.9	-6.3	-6.4	-1.8	-12.9	-21.6	-12.7	-5.7	-3.7

Source: Forecast produced using Laurence H. Meyer and Associates' model of the U.S. economy.
Assumptions and simulations by Dr. John Tuccillo, Dr. Frederick Flick and Sean Burns.